

Discussion of “United States Inequality through the Prisms of Income  
and Consumption”

by

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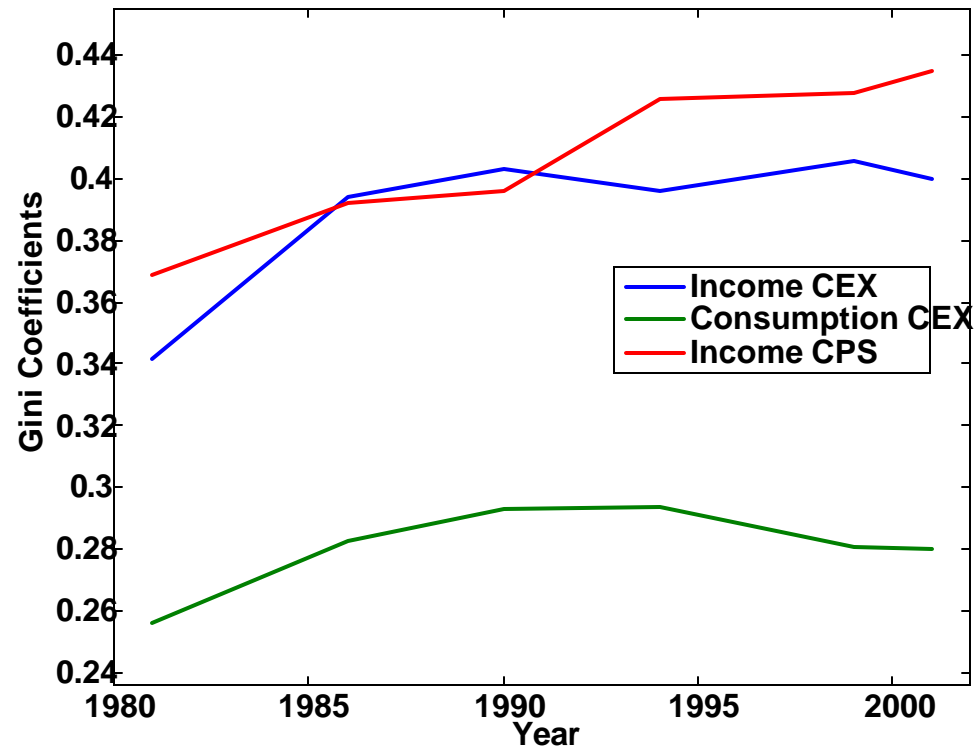
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## The Questions

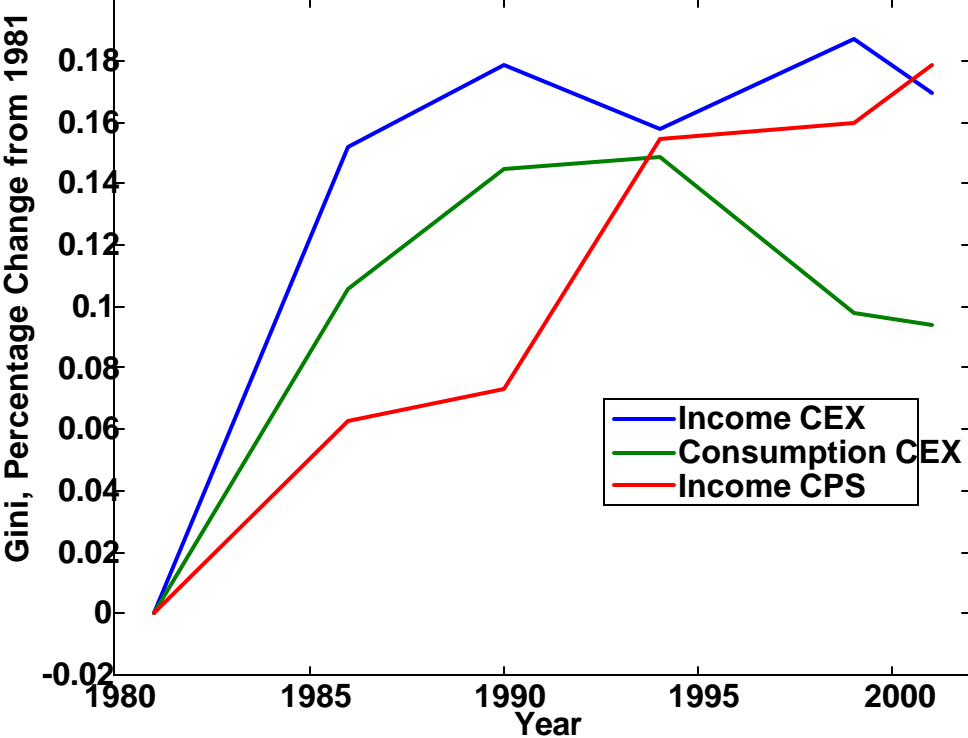
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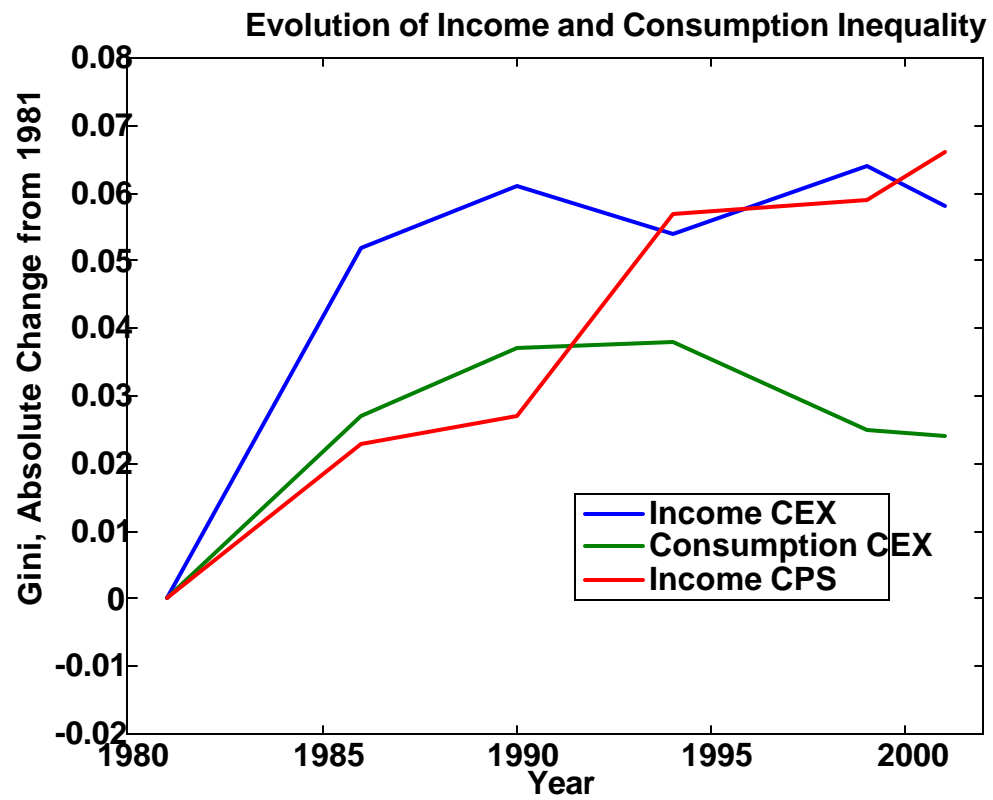
- Question: what has happened to economic inequality in the last 20 years?
- Does the answer depend on the economic variable that is being studied (disposable income vs. consumption)?
- Relative Performance of particular subgroups: a) the elderly, b) the children and their families, c) other groups of the population

Evolution of Income and Consumption Inequality

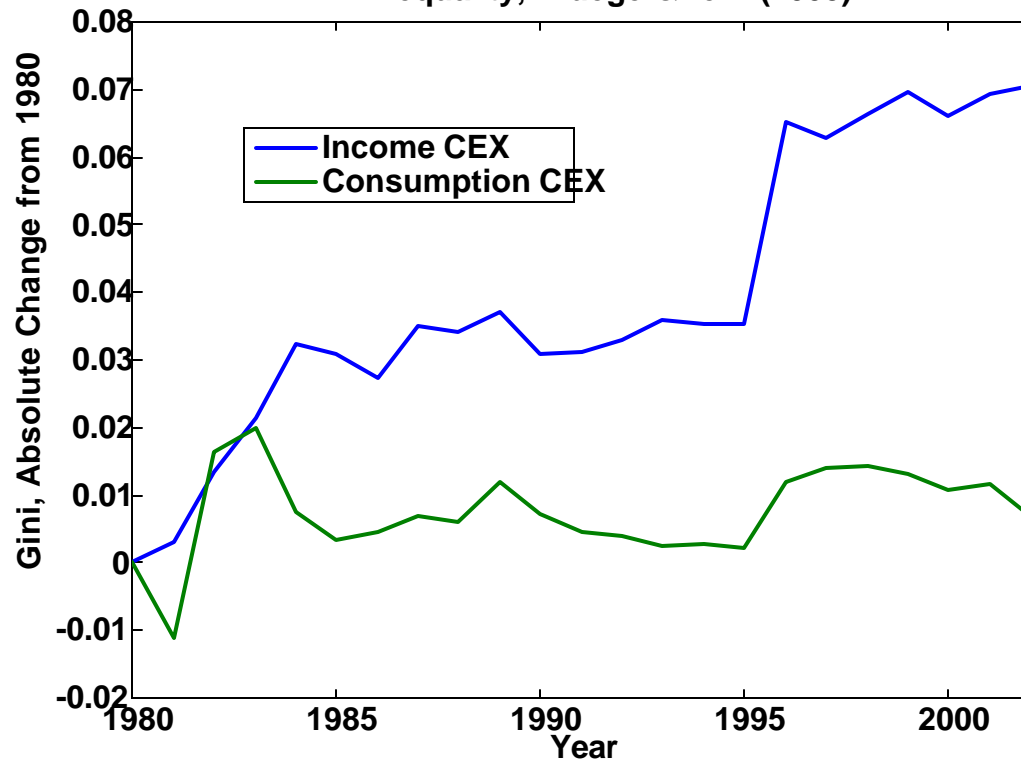


Evolution of Income and Consumption Inequality





Inequality, Krueger&Perri (2005)



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## Gini Coefficient vs. Variance of Logs

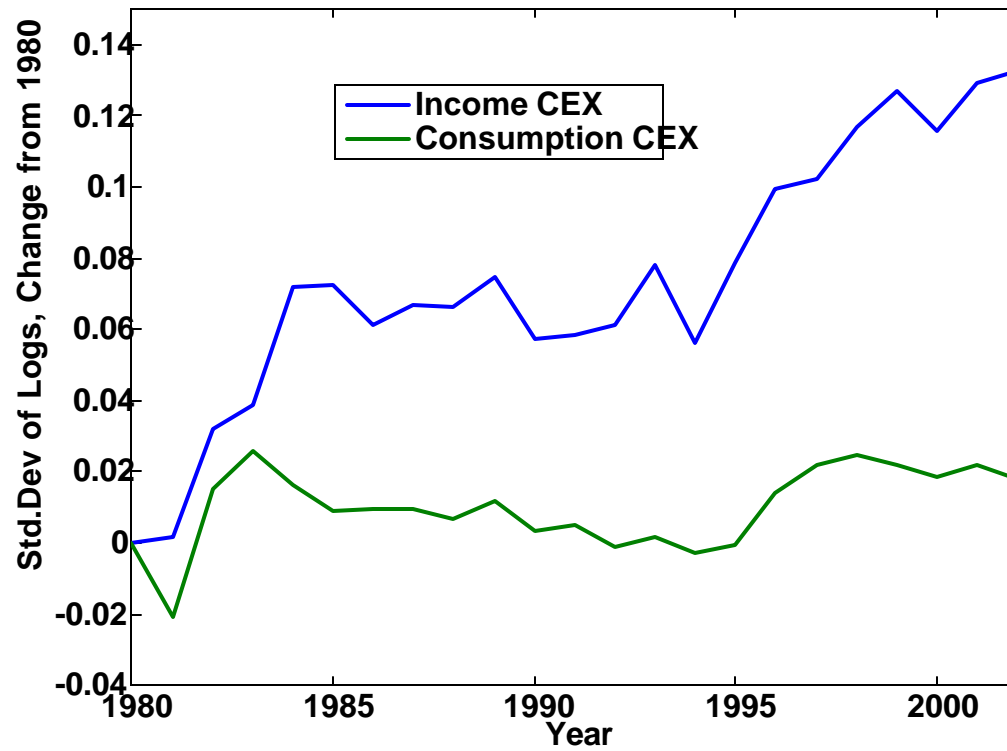
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- Interpretation in change of Gini: changes vs. percentage changes.
- Gini coefficient is not easily decomposable into between- and within-group inequality. If  $F$  is cross-sectional distribution,  $I(.)$  an inequality measure, it would be useful if

$$\begin{aligned} I(F) &= \sum_{j=1}^J \omega_j I(F^{(j)}) + I(F_\mu) \\ &= \underbrace{\sum_{j=1}^J \omega_j I(F^{(j)})}_{\text{Within Group}} + \underbrace{I(F_\mu)}_{\text{Between Groups}} \end{aligned}$$

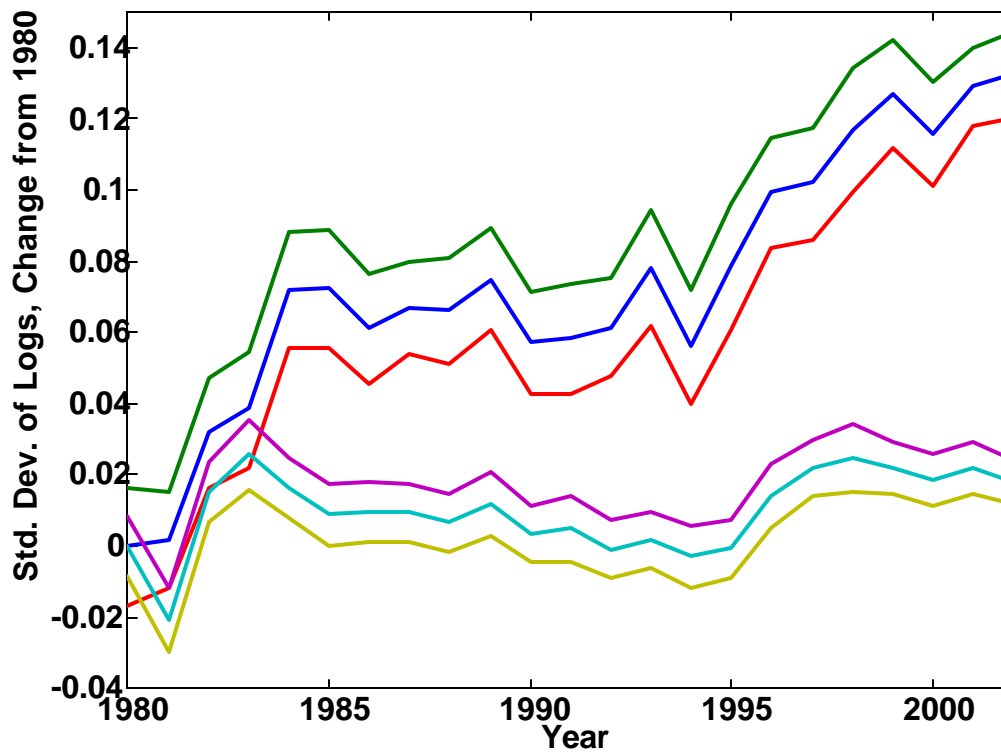
- The variance of logs does not have these problems.

Inequality, Krueger&Perri (2005)





Inequality, Krueger&Perri (2005)



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## Potential Explanations for Divergence

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- Changes in the population structure. But divergence persists after controlling for population structure.
- Deepening financial markets improve consumption insurance against transitory and persistent (but not permanent shocks). See Krueger and Perri (2004).
- Problems with quality of the CEX family data set. Somewhat different implications obtained with diary data (see Attanasio, Battistin and Ichimura, 2004).

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## Does Consumption Inequality Measure Welfare Inequality

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- Even from the cross-sectional distribution of individual consumption it is difficult to deduce properties of the cross-sectional distribution of welfare.
- Denote by  $c_{ia}$  consumption at age  $a$  of agent  $i$ , and by  $U_i$  expected lifetime utility of agent  $i$ . Agents can freely borrow and save at common (possibly time-varying) interest rate  $r_s$  and are only constrained by their lifetime budget constraint (i.e. the model underlying the permanent income hypothesis).
- Blundell and Preston (1999) show the following:

1. Suppose one observes agents  $i$  and  $j$  at the same time and they share the same birth year. Then

$$c_{ia} \geq c_{ja} \Leftrightarrow U_i \geq U_j$$

if and only if consumption in all periods of life is a normal good.

2. Suppose one observes agents  $i$  and  $j$  at the same time and they do *not* share the same birth year (i.e. are of different age at the time of observation). Then

$$c_{ia} \geq c_{j\hat{a}} \Leftrightarrow U_i \geq U_j$$

if and only if  $U(c_1, c_2, \dots, c_T) = \min_a u(c_{ia})$ , where  $u$  is an increasing function.

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## Conclusion

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- A very nice paper about an important issue.
- Do income and consumption data really show the same picture for the change in economic inequality?
- Important to settle this question because of policy implications of the answer.
- What can we say about welfare?

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## Conclusion

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There is a surprising difference between the trends in the dispersion of holdings of claims to goods and services (income and wealth) and trends in the dispersion of actual consumption, which is, of course, the ultimate determinant of material or economic well-being [Alan Greenspan (1996)]